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ALLEGHENY GENERAL HOSPITAL

CONSOLIDATING STATEMENT OF OPERATIONS

For the year ended June 30, 1996

(Dollars in Thousands)

	AGH	ASRI	Consolidated AGH
Unrestricted revenues, gains and other support:			
Net patient service	\$394,561	\$ -	\$ 394,561
Research support		8,789	8,789
Investment income	22,960	331	23,291
Net assets released from restrictions used for operations	6,838	1,680	8,518
Other revenue	22,168	1,813	23,981
Total revenues, gains and other support	446,527	12,613	459,140
Expenses:			
Salaries, wages and fringe benefits	195,809	8,704	204,513
Materials, supplies and services	185,632	16,030	201,662
Depreciation and amortization	31,233	2,051	33,284
Interest	13,919	8	13,927
Unusual items	3,149	-	3,149
Total expenses	429,742	26,793	456,535
Net income/(loss), before change in accounting principles	16,785	(14,180)	2,605
Income from change in accounting principles	3,716	-	3,716
Net income/(loss)	20,501	(14,180)	6,321
Transfers (to)/from affiliates, net	(33,629)	19,471	(14,158)
Transfers from deferred revenue	-	562	562
Net assets released from restrictions used for acquisition of property and equipment	81	1,010	1,091
Increase/(decrease) in unrestricted net assets	\$ (13,047)	\$ 6,863	\$ (6,184)

**Allegheny Health, Education and Research Foundation**  
**Delaware Valley Obligated Group**

*Combined  
Financial  
Statements  
for the  
year ended  
June 30, 1996*

**GOV 56000**

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**Coopers  
& Lybrand**

Coopers &amp; Lybrand L.L.P.

a professional services firm

**Report of Independent Accountants**

To the Boards of Trustees of  
Allegheny University Hospitals,  
Allegheny University of the Health Sciences  
and St. Christopher's Hospital for Children:

We have audited the accompanying combined balance sheet of the Allegheny Health, Education and Research Foundation Delaware Valley Obligated Group (the Obligated Group) as of June 30, 1996, and the related combined statements of operations, changes in net assets, and cash flows for the year then ended. These combined financial statements are the responsibility of the Obligated Group's management. Our responsibility is to express an opinion on these combined financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the combined financial position of the Allegheny Health, Education and Research Foundation Delaware Valley Obligated Group as of June 30, 1996 and the combined results of its operations, changes in net assets and cash flows for the year then ended in conformity with generally accepted accounting principles.

As discussed in Note 2 to the combined financial statements, the Allegheny Health, Education and Research Foundation Delaware Valley Obligated Group changed its method of accounting for contributions by adopting Statement of Financial Accounting Standards (SFAS) No. 116, "Accounting for Contributions Received and Contributions Made" and its method of reporting by adopting SFAS No. 117, "Financial Statements of Not-for-Profit Organizations," as well as its method of accounting for investments by adopting SFAS No. 124, "Accounting for Certain Investments Held by Not-for-Profit Organizations."

Pittsburgh, Pennsylvania  
September 11, 1996

*Coopers & Lybrand L.L.P.*

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ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

COMBINED BALANCE SHEET

June 30, 1996

(Dollars in Thousands)

ASSETS

Current assets:	
Cash and cash equivalents	\$ 27,282
Assets limited or restricted as to use	24,039
Receivables:	
Patient accounts, less allowance for uncollectible accounts of \$50,625	252,568
Grants and other	37,906
Inventories	12,749
Prepaid expenses	<u>3,380</u>
Total current assets	357,924
Assets limited or restricted as to use, net of current portion	157,772
Property and equipment, net	419,945
Other assets	<u>23,153</u>
Total assets	\$ <u>958,794</u>

LIABILITIES AND NET ASSETS

Current liabilities:	
Accounts payable and accrued expenses	\$ 114,760
Payable to affiliates	21,076
Self-insurance liabilities	3,848
Deferred revenue	13,323
Lines of credit	40,300
Current portion of long-term debt	<u>690</u>
Total current liabilities	193,997
Long-term debt, net of current portion	406,450
Student loans	18,731
Payable to affiliates	60,797
Self-insurance liabilities	9,430
Other noncurrent liabilities	<u>1,168</u>
Total liabilities	690,573
Net assets:	
Unrestricted	150,925
Restricted:	
Temporarily	50,053
Permanently	<u>67,243</u>
Total net assets	<u>268,221</u>
Total liabilities and net assets	\$ <u>958,794</u>

The accompanying notes are an integral part of the combined financial statements.

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ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

COMBINED STATEMENT OF OPERATIONS  
For the year ended June 30, 1996  
(Dollars in Thousands)

Unrestricted revenues, gains and other support:	
Net patient service revenue	\$ 883,816
Research and training support	51,446
Academic activities	62,916
Other revenue	49,999
Investment income	17,588
Net assets released from restrictions used for operations	<u>10,398</u>
Total revenues, gains and other support	<u>1,076,163</u>
Expenses:	
Salaries, wages and fringe benefits	597,645
Materials, supplies and services	374,315
Depreciation and amortization	50,339
Interest	<u>26,984</u>
Total expenses	<u>1,049,283</u>
Net income, before extraordinary item and change in accounting principle	26,880
Extraordinary loss on early extinguishment of debt	(32,534)
Income from change in accounting principle	<u>4,363</u>
Net loss	(1,291)
Net assets released from restrictions used for acquisition of property and equipment	1,715
Transfers from other net assets	971
Transfers to affiliates, net	<u>(73,676)</u>
Decrease in unrestricted net assets	\$ <u>(72,281)</u>

The accompanying notes are an integral part of the combined financial statements.

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

COMBINED STATEMENT OF CHANGES IN NET ASSETS

For the year ended June 30, 1996

(Dollars in Thousands)

Unrestricted net assets:	
Net loss	\$ (1,291)
Net assets released from restrictions used for acquisition of property and equipment	1,715
Transfers from other net assets	971
Transfers to affiliates, net	<u>(73,676)</u>
Decrease in unrestricted net assets	<u>(72,281)</u>
Temporarily restricted net assets:	
Adjustment from change in accounting principles	7,183
Contributions	4,991
Investment income	6,592
Unrealized appreciation of investments	3,570
Net assets released from restrictions	(13,396)
Transfers to other net assets	(550)
Transfers from affiliates	<u>111</u>
Increase in temporarily restricted net assets	<u>8,501</u>
Permanently restricted net assets:	
Adjustment from change in accounting principles	13,999
Contributions	4,976
Investment income	284
Unrealized appreciation of investments	527
Transfers from affiliates	1,594
Transfers to other net assets	<u>(421)</u>
Increase in permanently restricted net assets	<u>20,959</u>
Decrease in net assets	(42,821)
Net assets, beginning of year	<u>311,042</u>
Net assets, end of year	\$ <u>268,221</u>

The accompanying notes are an integral part of the combined financial statements.

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ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

COMBINED STATEMENT OF CASH FLOWS

For the year ended June 30, 1996

(Dollars in Thousands)

Cash flows from operating activities:	
Change in net assets	\$ (42,821)
Adjustments to reconcile changes in net assets to net cash provided by operating activities:	
Extraordinary loss on early extinguishment of debt	32,534
Adjustment from change in accounting principles	(25,545)
Depreciation and amortization	50,339
Net transfers to affiliates	71,971
Net unrealized appreciation of investments	(10,399)
Increase/(decrease) in cash and cash equivalents from changes in:	
Patient receivables	(72,228)
Intercompany accounts	45,230
Other current assets	(11,487)
Accounts payable and accrued expenses	34,777
Other	(22,217)
Net cash provided by operating activities	<u>50,154</u>
Cash flows from investing activities:	
Acquisition of property and equipment, net	(71,666)
Decrease in assets limited or restricted as to use, net	<u>68,423</u>
Net cash used by investing activities	<u>(3,243)</u>
Cash flows from financing activities:	
Issuance of long-term debt	404,834
Early extinguishment of long-term debt	(369,636)
Net borrowings under lines of credit	34,300
Repayment of long-term debt	(7,492)
Payment of debt issuance costs	(9,664)
Net transfers to affiliates	<u>(71,971)</u>
Net cash used by financing activities	<u>(19,629)</u>
Net increase in cash and cash equivalents	27,282
Cash and cash equivalents, beginning of year	<u>-</u>
Cash and cash equivalents, end of year	\$ <u>27,282</u>
Supplemental disclosure:	
Cash paid for interest	\$ <u>36,190</u>

The accompanying notes are an integral part of the combined financial statements.

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996  
(Dollars in Thousands)

1. Organization:

The Allegheny Health, Education and Research Foundation (AHERF) Delaware Valley Obligated Group (the Obligated Group) financial statements provide combined financial information about the organizations that are obligated in connection with the issuance of the Series 1996 Bonds by the Pennsylvania Higher Educational Facilities Authority (the Authority).

The Obligated Group consists of Allegheny University of the Health Sciences (Allegheny University), Allegheny University Hospitals and St. Christopher's Hospital for Children (St. Christopher's), collectively referred to as "Members" of the Obligated Group.

Allegheny University owns and operates a health sciences university currently comprised of a medical school, undergraduate and graduate schools of health sciences and humanities, various physician group practices and research activities, principally located in Philadelphia, Pennsylvania. Allegheny University is the parent company of Hahnemann Insurance Company, Inc. (HAHN), a nonprofit captive insurance company incorporated under the insurance laws of the state of Vermont. Allegheny University Hospitals owns and operates two tertiary care teaching hospitals (Allegheny Center City Hospital and Allegheny East Falls Hospital) and two acute care community hospitals (Allegheny Bucks County Hospital and Allegheny Elkins Park Hospital) in Philadelphia, Pennsylvania. Additionally, Allegheny University Hospitals, operate on behalf of the Commonwealth of Pennsylvania, an inpatient psychiatric facility (Eastern Pennsylvania Psychiatric Institute) for adults and children located in Philadelphia, Pennsylvania. St. Christopher's is an acute care children's hospital and a regional referral center located in Philadelphia, Pennsylvania.

Each of the Members of the Obligated Group is a controlled affiliate of AHERF and a Pennsylvania nonprofit corporation, exempt from federal income taxation. AHERF, a nonprofit organization, is also the parent company of Allegheny General Hospital (AGH), Allegheny Integrated Health Group, Allegheny Health Services Providers Insurance Company (AHSPIC), and Diversified Health Group, Inc. (DHG). AGH is the parent company of Allegheny-Singer Research Institute (ASRI).



ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

1. Organization: (continued)

The Series 1996 Bonds were issued by the Authority under a Bond Indenture. The proceeds therefrom were applied, together with other funds available to the Members of the Obligated Group, principally to undertake a program to refinance certain obligations of the Members. In connection with the issuance of the Series 1996 Bonds, Allegheny University Hospitals, Allegheny University and St. Christopher's became members of the Obligated Group.

2. Accounting Policies:

The significant accounting policies applied in preparing the accompanying combined financial statements are summarized below:

Principles of Combination:

The accompanying combined financial statements include the accounts of Allegheny University Hospitals, Allegheny University and St. Christopher's. All intercompany transactions have been eliminated in combination.

Accounting Changes:

In fiscal year 1996, the Obligated Group adopted Financial Accounting Standards Board Statements (FAS), No. 116, "Accounting for Contributions Received and Contributions Made," No. 117, "Financial Statements of Not-for-Profit Organizations" and No. 124, "Accounting for Certain Investments Held by Not-for-Profit Organizations." FAS 116 requires that unconditional promises by donors to pledge monies to the Obligated Group be recorded as receivables and revenues within the appropriate net asset category. FAS 116 also requires that any perpetual trusts held and administered by third parties, of which the not-for-profit organization is the beneficiary, be recorded as a contribution to permanently restricted assets measured by the fair value of the assets contributed. As permitted by FAS 116, the cumulative effect of adopting this statement for periods prior to July 1, 1995 is \$2,549 and \$13,673 for temporarily and permanently restricted funds, respectively, and are reflected as adjustments from change in accounting

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)

principles on the combined statement of changes in net assets. FAS 117 establishes uniform standards for general-purpose external financial statements of not-for-profit organizations. FAS 117 further requires the classification of net assets into three categories, based on the existence or absence of donor-imposed restrictions as follows:

Unrestricted - Net assets that are not subject to donor-imposed stipulations. Such net assets may be designated by the Boards of Trustees for specific purposes or limited by contractual agreements with outside parties.

Temporarily Restricted - Net assets whose use is subject to donor-imposed stipulations that can be fulfilled by specific actions pursuant to such stipulations or expire by the passage of time.

Permanently Restricted - Net assets subject to donor-imposed stipulations that neither expire by passage of time nor can be fulfilled and removed by action. Such net assets, which must be maintained in perpetuity, generally include only the original amount of the contribution since the donors of these assets most often permit the use of all investment earnings for specific or general purposes.

FAS 124 requires that investments in equity securities with readily determinable fair values and all investments in debt securities be reported at fair value with gains and losses included in the combined statement of operations. As permitted by FAS 124, the cumulative effect of adopting this statement for periods prior to July 1, 1995 is \$4,363 for unrestricted investments, which is reflected as an adjustment from change in accounting principle on the combined statement of operations, and \$4,634 and \$326 for investments temporarily and permanently restricted, respectively, which are reflected on the combined statement of changes in net assets.

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)

Use of Estimates:

The preparation of these combined financial statements in conformity with generally accepted accounting principles requires the Obligated Group's management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the combined financial statements. Estimates also affect the amounts reported as revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents:

Cash and cash equivalents include highly liquid investments purchased with a maturity date of three months or less and deposits maintained with AHERF which are available to the Obligated Group.

Investments and Investment Income:

The Obligated Group's investments are carried at fair value and consist generally of certificates of deposit, government and corporate obligations that have fixed rates of return, pooled investment funds and marketable equity securities of domestic companies.

Donated investments are recorded at estimated fair value at the date of contribution. Unrestricted investment income and gains and losses on sales of investments, which are based on average cost, are included in investment income.

Grants Receivable and Deferred Revenue:

Grants and contracts are recognized in the year in which expenditures are made, either as research support or, in the case of expenditures for property and equipment, as additions to net assets. Receivables are recorded when contract and grant expenditures exceed funds received. Deferrals are recorded when funds received are in excess of expenditures incurred. Additionally, notices of federal and other research grant awards relating to future years have not been recorded.

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)

Inventories:

Inventories are valued at the lower of average cost or fair value.

Property and Equipment:

Property and equipment, along with expenditures that extend the useful lives of assets, are recorded at cost. Certain internal computer software development costs are capitalized and included in property and equipment. Interest is capitalized in accordance with the construction of major capital additions. Maintenance and repairs are charged to expense as incurred. At the time assets are retired or otherwise disposed of, the cost thereof and accumulated depreciation or amortization are eliminated and any resulting gain or loss on disposition is recorded as other revenue.

Depreciation is provided over the estimated useful lives of the assets computed under the straight-line method with one-half year of depreciation recognized in the year the related assets are placed into service.

Other Assets:

Other assets consist primarily of bond financing costs, equity investments and program development costs. Bond financing costs are being amortized over the respective terms of the related bond issues on a basis that approximates the interest method. Program development costs are being amortized over three years under the straight line method.

Restricted Net Assets:

Temporarily restricted net assets are those whose use has been limited by donors for a specific purpose or a specific time period. Permanently restricted net assets have been restricted by donors to be maintained in perpetuity. Temporarily restricted assets released from restriction during the period are reflected in the combined statement of operations.

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)

Net Patient Service Revenue:

The Obligated Group's hospitals have agreements with third-party payors that provide for payments to Obligated Group facilities at amounts different from their established rates. Payment arrangements include prospectively determined rates based upon discharges, discounted charges, per diem payments and capitation arrangements. Net patient service revenue is reported at the estimated net realizable amounts due from patients, third-party payors, and others for services rendered, including estimated net retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.

Charity Care, Uncompensated Care and Other Community Services:

The Obligated Group's hospitals maintain charity care policies which were established to assure that all persons seeking treatment receive needed health care services regardless of their ability to pay. These policies provide that persons who lack the means to pay for all or a portion of their needed health care services receive financial assistance in the form of partial or total charge reductions. Because the hospitals do not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. The amount of charges forgone for services and supplies furnished under the Obligated Group's charity care policy approximated \$9,956 in fiscal year 1996.

Additionally, the Obligated Group's hospitals provide services to patients covered by Medical Assistance and Medicare, whereby the payments received are less than the cost of providing such services. Also, the Obligated Group's hospitals perform services at no charge which benefit the community, such as public health screenings, health care publications, workplace wellness programs, health related research, educational programs and other activities.

**ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP**

**NOTES TO COMBINED FINANCIAL STATEMENTS**

June 30, 1996

(Dollars in Thousands)

**2. Accounting Policies: (continued)**

**Related Party Transactions:**

Fees charged for services provided by affiliates are included in expenses with all other transactions among affiliates recorded as net asset transfers. Any resulting accounts receivable or payable with affiliates are settled periodically in the normal course of business.

**Income Taxes:**

The members of the Obligated Group are not-for-profit corporations that have been recognized as tax exempt pursuant to Section 501 (c)(3) of the Internal Revenue Code.

**3. Assets Limited or Restricted as to Use:**

Assets limited or restricted as to use consist of the following components at June 30, 1996:

**Unrestricted:**

**By Boards of Trustees:**

Future additions to or replacement of property and equipment	\$ 5,602
Self-insurance reserve funds	6,154
Endowments	25,899
Other	<u>8,925</u>

46,580

**By Financing Agreements**

Endowments	3,495
	<u>8,408</u>

58,483

**Temporarily restricted:**

Endowments	32,419
Student loans	19,230
By donor	<u>8,078</u>

59,727

**Permanently restricted:**

Endowments	51,807
Perpetual trusts	<u>11,794</u>

63,601

Total assets limited or restricted as to use	181,811
Less current portion	<u>24,039</u>

Assets limited or restricted as to use \$ 157,772

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996  
(Dollars in Thousands)

3. Assets Limited or Restricted as to Use: (continued)

The following table sets forth the composition of assets limited or restricted as to use by investment type at June 30, 1996:

Unrestricted:

Cash and short-term investments	\$ 9,635
Government and corporate obligations	31,328
Marketable equity securities	<u>17,520</u>
	58,483

Temporarily restricted:

Cash and short-term investments	23,713
Government and corporate obligations	23,163
Marketable equity securities	<u>12,851</u>
	59,727

Permanently restricted:

Cash and short-term investments	1,859
Government and corporate obligations	34,220
Marketable equity securities	<u>27,522</u>
	63,601

Assets limited or restricted as to use	<u>\$ 181,811</u>
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The Obligated Group's various Boards of Trustees retain control over certain designated assets and may, at their discretion, subsequently use such assets for other purposes. Assets limited or restricted as to use, including \$5,151 of temporarily restricted funds that are required to satisfy obligations classified as current liabilities, are reported as current assets on the combined balance sheet.

Investment returns consisted of the following for the year ended June 30, 1996:

Net gains on investments	\$ 7,692
Dividends and interest	<u>4,921</u>
	<u>\$ 12,613</u>

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

4. Property and Equipment:

Property and equipment consists of the following components at June 30, 1996:

Buildings and building improvements	\$ 382,157
Equipment	393,315
Land and land improvements	<u>23,948</u>
	799,420
Less accumulated depreciation and amortization	<u>421,940</u>
	377,480
Construction in progress	<u>42,465</u>
	<u>\$ 419,945</u>
Property and equipment, net	

5. Lines of Credit:

The Obligated Group maintains \$58,000 of working capital lines of credit from several banks with various maturity dates through November 1997 and interest at variable rates ranging from 6.3% to 9.0% during fiscal year 1996 and 6.4% to 6.8% at June 30, 1996. Amounts outstanding under these lines of credit were \$40,300 at June 30, 1996.

6. Long-Term Debt:

Long-term debt consists of the following obligations at June 30, 1996:

Pennsylvania Higher Educational Facilities Authority (PHEFA):

Revenue Bonds:

Series 1996 A-C, net of unamortized discount of \$3,606 (with maturity dates through November 15, 2021 and fixed interest rates ranging from 4.0% to 5.9%)	\$ 302,544
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Series 1996 Variable Rate Bonds (with maturity dates through November 15, 2035 and a variable rate of 5.43% on June 30, 1996)	50,000
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Notes payable (with maturity dates through November 15, 2015 and a variable rate of 3.45% on June 30, 1996)	52,290
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Other obligations	<u>2,306</u>
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	407,140
Less amounts maturing within one year	<u>690</u>

Long-term debt	<u>\$ 406,450</u>
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ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

6. Long-Term Debt: (continued)

In June 1996, \$306,150 of PHEFA Health Services Revenue Bonds Series A-C, \$50,000 of PHEFA Variable Rate Bonds and \$52,290 of PHEFA notes payable were issued to refinance certain obligations of the Obligated Group and to reimburse the Obligated Group for certain construction, renovation and equipment purchases. A portion of the proceeds, along with certain funds held under prior bond indentures, were deposited into irrevocable escrow accounts invested in federal government obligations scheduled to mature and pay interest in amounts sufficient to meet all debt service requirements for the refunded obligations. The escrow funds along with refunded obligations are not included on the Obligated Group's combined balance sheet. The outstanding principal balance of the refunded obligations was \$342,283 at June 30, 1996.

As a result of the fiscal year 1996 advance refunding, an extraordinary loss of \$32,534 was recognized, which represents the difference between the reacquisition cost and the carrying amount of the refunded bonds, adjusted for accrued interest and deferred financing costs.

All long-term debt is subject to early redemption at the option of the Obligated Group. Additionally, the Obligated Group is subject to various debt covenants contained in the Master Trust Indenture and Loan and Security Agreements which govern the preceding obligations. The most restrictive of these covenants require the Obligated Group to maintain minimum long-term debt service coverage and liquidity ratios. Additionally, the bonds are collateralized by the pledge of certain of the Obligated Group's gross revenue, real property, personal property and accounts receivable.

Following are scheduled principal repayments and sinking fund requirements on the long-term debt for each of the next five fiscal years:

1997 -	\$ 690
1998 -	11,766
1999 -	10,735
2000 -	11,290
2001 -	11,825

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996  
(Dollars in Thousands)

7. Commitments:

Effective July 1, 1989, the Obligated Group entered into an operating lease agreement with the Commonwealth of Pennsylvania whereby all land and buildings associated with the Eastern Pennsylvania Psychiatric Institute are leased for a term of 25 years at annual rental payments of one dollar. The agreement also specifies provisions for a renewal option for additional terms.

Certain office space adjacent to St. Christopher's is subleased to a medical university, which has a teaching affiliation with St. Christopher's, for use as professional office space for the medical faculty and students of that university. The sublease currently provides annual gross rental income of approximately \$1,700 and expires in March, 2000.

The Obligated Group leases certain medical and office equipment and office space used in its operations. Rental expense for operating leases for the year ended June 30, 1996 was \$13,631. The annual and total future minimum lease payments under noncancelable operating leases entered into as of June 30, 1996 are as follows:

<u>Year</u>	
1997	\$ 6,130
1998	3,948
1999	3,510
2000	2,997
2001	2,730
2002 and thereafter	<u>19,549</u>
Total minimum payments	<u>\$ 38,864</u>

8. Net Patient Service Revenue:

Net patient service revenue consists of the following components for the year ended June 30, 1996:

Gross patient service revenue	\$ 2,245,999
Less provisions for contractual adjustments	<u>1,362,183</u>
Net patient service revenue	<u>\$ 883,816</u>

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

8. Net Patient Service Revenue: (continued)

Contractual adjustments represent the difference between standard billing rates and amounts estimated to be paid under various health benefit agreements. Provisions for contractual adjustments are recorded in the period in which the services are provided.

During fiscal year 1996, the Obligated Group's bad debt expense amounted to \$49,523, which is included in materials, supplies and services expense on the combined statement of operations.

9. Insurance:

AHERF is self-insured for primary coverage and for certain levels of excess coverage related to professional and general liability claims through AHSPIC (an affiliated captive insurance company incorporated in the Cayman Islands), HAHN and various self insurance trusts. In addition, AHERF participates in the Medical Professional Liability Catastrophic Loss Fund of the Commonwealth of Pennsylvania (CAT Fund) and maintains insurance under commercially insured programs on a claims-made basis for amounts in excess of the self-insurance and CAT Fund coverages. Premiums for the self-insurance coverage are retrospectively rated and are paid to AHSPIC and HAHN based on funding requirements determined by independent insurance actuaries to include provisions for estimates for the ultimate costs for both reported claims and claims incurred but not reported, determined on a discounted basis using a 7.5% rate. Professional and general liability expense is allocated by AHERF to each relevant AHERF entity based principally upon such entity's reported claims and estimated claims incurred but not reported. During fiscal year 1996, the Obligated Group's total professional and general liability insurance expense was \$20,708.

HAHN was formed in December 1991 to provide professional liability insurance coverage for the former Hahnemann University, including its hospital, directors, officers, residents and non-physician employees. The insurance policy with HAHN was not renewed as of January 1, 1995 and AHSPIC commenced providing professional liability insurance coverage. HAHN's insurance business is now considered to be in run-off.

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996  
(Dollars in Thousands)

9. Insurance: (continued)

AHERF is also self-insured for workers' compensation liability claims and has established trust funds for the payment of such claims. Funding requirements and estimates of losses incurred are determined on a discounted basis using actuarial assumptions which include a 6.0% discount rate and which are subject to revision based upon actual experience. Workers' compensation expense is allocated by AHERF to each relevant AHERF entity based principally upon such entity's reported claims and estimated claims incurred but not reported. During fiscal year 1996, the Obligated Group's workers' compensation expense was \$6,225.

10. Pension Plans:

AHERF maintains a noncontributory, defined benefit pension plan covering substantially all Obligated Group employees. Under this cash balance plan (the Plan), pension accruals are determined using a defined percentage of an employee's current compensation based on the employee's age and years of service. Each employee's individual retirement benefit is defined within the Plan's obligation as a notational cash balance retirement account and is credited with interest based on a defined interest rate. AHERF's funding policy is to contribute such amounts as are necessary on an actuarial basis to provide the Plan with assets sufficient to meet benefits to be paid to retirees or their beneficiaries and to satisfy the minimum funding requirements of the Employee Retirement Income Security Act of 1974. Pension expense is allocated by AHERF to each relevant AHERF entity based principally upon the number of full and part time employees covered by the Plan and their respective salary levels. During fiscal year 1996, the Obligated Group's pension expense was \$9,894.

In addition, certain union employees are covered by multi-employer pension plans to which the Obligated Group contributes based on individual plan policies and actuarial valuations. Expenses in fiscal year 1996 pertaining to the multi-employer pension plans amounted to \$3,577.

AHERF sponsors a contributory, defined contribution savings plan which is available to substantially all Obligated Group employees in order to provide additional security during retirement by creating an incentive for employees to make regular contributions on their own behalf. Under this plan, and as determined on an individual employee basis, AHERF

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP

NOTES TO COMBINED FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

10. Pension Plans: (continued)

contributes an amount equal to 25% of an employee's contribution for employee contributions up to 4% of such employee's salary in a given year. Such expense is allocated by AHERF to each relevant AHERF entity based on actual contributions made. The Obligated Group's expense associated with contributions to this savings plan was \$1,932 for the year ended June 30, 1996.

11. Related Party Transactions:

AHERF provides selected management, administrative and support services to its operating units and charges them for these services. During fiscal year 1996, the Obligated Group incurred service charges from AHERF of \$151,091. These charges are included on the combined statement of operations as salaries, wages and fringe benefit expense and materials, supplies and services expense. Additionally, AHERF provided support under a matching endowment program of \$1,705 in fiscal year 1996. The matched endowments are recorded as restricted net assets on the combined balance sheet.

An affiliation agreement between AHERF and Allegheny University stipulates certain AHERF financial commitments to strengthen Allegheny University's academic, research and health services programs. Such financial support of operations, which is determined annually based upon Allegheny University's needs and available funds within the AHERF system, amounted to \$2,500 in fiscal year 1996. This agreement also specifies that AHERF will provide Allegheny University with a research grant, which is determined annually based upon the amount of external, competitively awarded research funds obtained by Allegheny University during the prior fiscal year and the total amount of internal funding available for research within the AHERF system. This research grant amounted to \$3,571 in fiscal year 1996. The support of operations is recorded as other revenue on the combined statement of operations. The amounts pertaining to the research grant are initially recorded as deferred revenue on the combined balance sheet and subsequently reflected as research and training support on the combined statement of operations as the related research expenses are incurred.

During fiscal year 1996, the Obligated Group charged AGH \$16,536 for clinical, teaching, research and administrative services of certain employed physicians. The fees charged for these physician services are included in other revenue on the combined statement of operations.

**ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP**

**NOTES TO COMBINED FINANCIAL STATEMENTS**

June 30, 1996

(Dollars in Thousands)

**11. Related Party Transactions: (continued)**

During fiscal year 1996, the Obligated Group charged Allegheny Integrated Health Group \$58,119 for clinical and administrative services in connection with the operations of physician practices. Such amounts are reflected on the combined statement of operations as a reduction of salaries, wages and fringe benefit expense. Also, during fiscal year 1996, the Obligated Group, through AHERF, transferred \$50,499 to Allegheny Integrated Health Group to support its acquisition and operation of physician practices. These transfers have been reflected as net asset transfers to affiliates on the combined statement of changes in net assets. Prior to fiscal year 1996, support of Allegheny Integrated Health Group's operations was provided through expense subsidization, which was reflected as an expense on the combined statement of operations as opposed to a net asset transfer.

**12. Functional Expenses:**

The Obligated Group provides general health care services through its hospitals and provides education services and performs medical research through its university. Expenses related to these services are as follows for the year ended June 30, 1996:

Health care services	\$ 835,613
Education services	76,534
Medical research	51,844
General and administrative	85,292
	<u>\$ 1,049,283</u>

**13. Concentration of Credit Risk:**

The Obligated Group's hospitals grant credit without collateral to its patients, most of whom are local residents who are insured under third-party payor agreements. The mix of receivables from patients and third-party payors is as follows at June 30, 1996:

Medicare	16%
Medicaid	26
Blue Cross	12
Managed Care	25
Other third-party payors	13
Patients	8
	<u>100%</u>

ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP  
NOTES TO COMBINED FINANCIAL STATEMENTS  
June 30, 1996  
(Dollars in Thousands)

14. Fair Value of Financial Instruments:

The following methods and assumptions were used by the Obligated Group in estimating the fair value of its financial instruments:

**Cash and cash equivalents:** The carrying value reported in the combined balance sheet for cash and cash equivalents approximates its fair value.

**Assets limited or restricted as to use:** These assets consist primarily of government and corporate obligations, marketable equity securities, cash and short-term investments. For government and corporate obligations and marketable equity securities, fair values were determined based on quoted market prices and dealer quotes where available, or quoted market prices pertaining to similar securities where not available. The carrying value for cash and short-term investments approximates fair value. The carrying value reported on the combined balance sheet for all assets limited or restricted as to use approximates their fair value.

**Student loan receivables:** Determination of the fair value of student loan receivables, which are primarily federally sponsored student loans with U.S. Government mandated interest rates and repayment terms and subject to significant restrictions as to their transfer or disposition, could not be made without incurring excessive costs.

**Long-term debt:** The fair value of all obligations included in long-term debt is based on current traded values. The carrying and fair values of the Obligated Group's long-term debt obligations are \$407,140 and \$405,630, respectively, at June 30, 1996.

15. Legal Matters:

The Obligated Group is subject to legal proceedings and claims which have arisen in the ordinary course of its business and have not yet been adjudicated. The ultimate liability from these actions cannot be determined because of the uncertainties that exist. In the opinion of management, the eventual disposition of these matters will not have a material adverse effect on the combined financial position of the Obligated Group. However, it is possible that, upon settlement, results of operations in a particular period could be materially affected.



**Coopers  
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**Report of Independent Accountants on Combining Financial Information**

Our report on the audit of the combined financial statements of the Allegheny Health, Education and Research Foundation Delaware Valley Obligated Group as of June 30, 1996, and for the year then ended appears on page 1. This audit was conducted for the purpose of forming an opinion on the combined financial statements taken as whole. The supplementary combining financial information accompanying the combined financial statements is not necessary for fair presentation of the combined financial position, results of operations and changes in net assets of the Allegheny Health, Education and Research Foundation Delaware Valley Obligated Group in conformity with generally accepted accounting principles. The supplementary combining financial information is presented only for purposes of additional analysis and is not a required part of the combined financial statements. The supplementary combining financial information has been subjected to the auditing procedures applied in the audit of the combined financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the combined financial statements taken as a whole.

*Coopers & Lybrand L.L.P.*

Pittsburgh, Pennsylvania  
September 11, 1996



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**ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP**

**COMBINING BALANCE SHEET  
as of June 30, 1996  
(Dollars in Thousands)**

	Allegheny East Falls Hospital	Allegheny Ethna Park Hospital	Allegheny Buena County Hospital	Allegheny Center City Hospital	Mgmt. Support Services	Total Allegheny University Hospitals	St. Christopher's	Allegheny University	Elim.	Combined AHERF - DV Obligated Grp.
<b>Current assets:</b>										
Cash and cash equivalents	\$ 4,215	\$ 1,039	\$ 1,070	\$ 5,068	\$ 199	\$ 11,591	\$ 14,943	\$ 748	\$ -	\$ 27,282
Assets limited or restricted as to use	1,457	-	-	8,426	10	9,893	1,943	12,203	-	24,039
Receivables:										
Patient accounts, net	58,450	21,288	17,012	78,534	-	175,284	43,319	33,963	-	252,568
Grants and other	1,936	177	43	2,483	57	4,696	9,953	23,257	-	37,906
From affiliates	-	-	-	-	-	7	-	306	(313)	-
Investor fees	2,909	666	577	6,549	209	10,910	1,839	-	-	12,749
Prepaid expenses	803	191	341	1,237	134	2,706	413	239	-	3,380
<b>Total current assets</b>	<b>69,770</b>	<b>23,361</b>	<b>19,043</b>	<b>102,304</b>	<b>609</b>	<b>215,087</b>	<b>72,412</b>	<b>70,738</b>	<b>(313)</b>	<b>357,924</b>
<b>Assets limited or restricted as to use, net</b>	<b>5,383</b>	<b>25</b>	<b>-</b>	<b>28,282</b>	<b>-</b>	<b>33,690</b>	<b>23,672</b>	<b>100,410</b>	<b>-</b>	<b>157,772</b>
Property and equipment, net	70,452	23,349	19,035	167,816	9,338	291,990	64,124	63,831	-	419,945
Receivables from affiliates	-	-	-	13,615	5,410	19,025	120	-	(19,145)	-
Other assets	7,033	981	1,371	6,929	14	16,378	3,032	3,843	-	23,153
<b>Total assets</b>	<b>\$ 152,638</b>	<b>\$ 49,716</b>	<b>\$ 39,392</b>	<b>\$ 318,946</b>	<b>\$ 15,371</b>	<b>\$ 576,070</b>	<b>\$ 163,360</b>	<b>\$ 238,822</b>	<b>\$ (19,438)</b>	<b>\$ 958,794</b>
<b>Current liabilities:</b>										
Accounts payable and accrued expenses	\$ 21,266	\$ 5,396	\$ 4,187	\$ 31,302	\$ 3,977	\$ 66,128	\$ 24,906	\$ 23,726	\$ -	\$ 114,760
Payable to affiliates	12,921	2,000	2,000	-	-	16,921	4,468	-	(313)	21,076
Self-insurance liabilities	803	-	-	2,543	-	3,346	-	500	-	3,848
Deferred revenue	208	-	-	982	-	1,190	597	11,536	-	13,323
Lines of credit	11,000	-	-	11,000	12,300	34,300	-	6,000	-	40,300
Current portion of long-term debt	-	-	616	74	-	690	-	-	-	690
<b>Total current liabilities</b>	<b>46,200</b>	<b>7,396</b>	<b>6,803</b>	<b>45,901</b>	<b>16,277</b>	<b>122,577</b>	<b>29,971</b>	<b>41,762</b>	<b>(313)</b>	<b>193,997</b>
Long-term debt, net of current portion	59,209	60,841	20,317	182,638	-	323,005	47,400	36,045	-	406,450
Student loans	-	-	-	-	-	-	-	18,731	-	18,731
Payable to affiliates	-	23,584	16,085	-	-	39,669	-	40,273	(19,145)	60,797
Self-insurance liabilities	-	-	-	4,530	-	4,530	-	4,900	-	9,430
Other noncurrent liabilities	-	51	74	-	44	169	206	793	-	1,168
<b>Total liabilities</b>	<b>105,409</b>	<b>91,872</b>	<b>43,279</b>	<b>233,069</b>	<b>16,321</b>	<b>489,950</b>	<b>77,377</b>	<b>142,504</b>	<b>(19,438)</b>	<b>690,573</b>
<b>Net Assets:</b>										
Unrestricted	44,285	(42,359)	(3,904)	64,620	(949)	61,693	73,716	15,516	-	150,923
Temporarily	1,489	203	24	5,851	(1)	7,566	4,952	33,535	-	50,033
Permanently	1,453	-	-	15,406	-	16,861	3,115	47,267	-	67,243
<b>Total net assets</b>	<b>47,229</b>	<b>(42,156)</b>	<b>(3,880)</b>	<b>85,877</b>	<b>(950)</b>	<b>86,120</b>	<b>81,783</b>	<b>96,316</b>	<b>-</b>	<b>268,271</b>
<b>Total liabilities and net assets</b>	<b>\$ 152,638</b>	<b>\$ 49,716</b>	<b>\$ 39,392</b>	<b>\$ 318,946</b>	<b>\$ 15,371</b>	<b>\$ 576,070</b>	<b>\$ 163,360</b>	<b>\$ 238,822</b>	<b>\$ (19,438)</b>	<b>\$ 958,794</b>

**ALLEGHENY HEALTH, EDUCATION AND RESEARCH FOUNDATION  
DELAWARE VALLEY OBLIGATED GROUP**

**COMBINING STATEMENT OF OPERATIONS  
for the year ended June 30, 1996  
(Dollars in Thousands)**

	Allegheny East Falls Hospital	Allegheny Ellis Park Hospital	Allegheny Butts County Hospital	Allegheny Center City Hospital	Mgmt. Support Services	Total Allegheny University Hospitals	SL Christopher's	Allegheny University	Elim.	Combined AHERF - DV Obligated Grp.
Unrestricted revenues, gains and other support:										
Net patient service	\$ 189,593	\$ 57,798	\$ 47,933	\$ 322,470	\$ -	\$ 618,214	\$ 134,149	\$ 131,433	\$ -	\$ 883,116
Research and ending support	2,242	-	-	3,626	-	5,868	2,231	43,347	-	51,446
Academic activities	-	114	13	-	24	154	792	61,970	-	62,916
Other revenue	7,324	667	802	6,566	3,361	18,920	7,355	70,734	(47,030)	49,999
Investment income	4,460	192	78	6,472	(250)	10,932	3,199	3,437	-	17,588
Net assets released from restrictions used for operations	540	2	-	57	-	600	4,961	4,837	-	10,298
<b>Total revenues, gains and other support</b>	<b>204,762</b>	<b>58,774</b>	<b>48,846</b>	<b>339,191</b>	<b>3,135</b>	<b>634,708</b>	<b>152,687</b>	<b>315,798</b>	<b>(47,030)</b>	<b>1,076,163</b>
Expenses:										
Salaries, wages and fringe benefits	104,430	26,714	21,851	160,741	16,230	329,966	67,223	204,456	-	597,645
Materials, supplies and services	81,907	21,029	19,779	144,626	(18,537)	255,784	60,774	104,787	(47,030)	374,315
Depreciation and amortization	6,920	3,276	2,806	18,500	5,462	36,974	6,415	6,950	-	50,339
Interest	3,276	5,102	1,901	10,434	-	20,833	3,608	2,543	-	26,984
<b>Total expenses</b>	<b>199,643</b>	<b>56,121</b>	<b>46,337</b>	<b>334,321</b>	<b>3,135</b>	<b>639,537</b>	<b>138,020</b>	<b>318,736</b>	<b>(47,030)</b>	<b>1,049,283</b>
Net income/(loss), before extraordinary item and change in accounting principle	\$ 5,119	\$ 2,653	\$ 2,509	\$ 4,870	\$ -	\$ 15,151	\$ 14,667	\$ (2,938)	\$ -	\$ 26,880
Extraordinary loss on early extinguishment of debt	(3,716)	(6,550)	(2,186)	(12,830)	-	(25,282)	(4,344)	(2,908)	-	(32,534)
Income from change in accounting principle	26	237	88	2,083	-	2,434	765	1,144	-	4,363
<b>Net income/(loss)</b>	<b>1,429</b>	<b>(3,660)</b>	<b>411</b>	<b>(5,877)</b>	<b>-</b>	<b>(7,677)</b>	<b>11,088</b>	<b>(4,702)</b>	<b>-</b>	<b>(1,291)</b>
Net assets released from restrictions used for acquisition of property and equipment	(2)	101	-	-	-	99	135	1,481	-	1,715
Transfer (to)/from other net assets	77	-	-	-	1	78	1,294	(401)	-	971
Transfer (to)/from affiliates, net	(70,287)	(10,655)	(9,537)	(16,220)	68	(26,651)	(10,292)	(6,283)	-	(73,675)
<b>Increase/(decrease) in unrestricted net assets</b>	<b>\$ (15,783)</b>	<b>\$ (14,194)</b>	<b>\$ (9,146)</b>	<b>\$ (22,097)</b>	<b>\$ 69</b>	<b>\$ (64,151)</b>	<b>\$ 1,771</b>	<b>\$ (9,903)</b>	<b>\$ -</b>	<b>\$ (72,381)</b>

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**Allegheny Integrated Health Group**

*Financial  
Statements  
for the  
year ended  
June 30, 1996*

**GOV 56025**

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Report of Independent Accountants

To the Board of Trustees of  
Allegheny Integrated Health Group:

We have audited the accompanying balance sheet of Allegheny Integrated Health Group as of June 30, 1996 and the related statements of operations and changes in net assets, and cash flows for the year then ended. These financial statements are the responsibility of Allegheny Integrated Health Group's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Allegheny Integrated Health Group as of June 30, 1996 and the results of its operations, changes in net assets and cash flows for the year then ended in conformity with generally accepted accounting principles.

*Coopers & Lybrand L.L.P.*

Pittsburgh, Pennsylvania  
September 11, 1996

## ALLEGHENY INTEGRATED HEALTH GROUP

BALANCE SHEET  
June 30, 1996  
(Dollars in Thousands)

## ASSETS

Current assets:	
Cash and cash equivalents	\$ 93
Short-term investments	387
Receivables:	
Patient accounts, less allowance for uncollectible accounts of \$629	17,455
Other	381
Inventories	34
Prepaid expenses	<u>358</u>
Total current assets	18,708
Property and equipment, net	15,642
Other assets	<u>22,400</u>
Total assets	<u>\$ 56,750</u>

## LIABILITIES AND NET ASSETS

Current liabilities:	
Accounts payable and accrued expenses	\$ 5,774
Current portion of long-term debt	<u>1,096</u>
Total current liabilities	6,870
Payables to affiliates	<u>12,806</u>
Total liabilities	19,676
Unrestricted net assets	<u>37,074</u>
Total liabilities and net assets	<u>\$ 56,750</u>

The accompanying notes are an integral part of the financial statements.

ALLEGHENY INTEGRATED HEALTH GROUP

STATEMENT OF OPERATIONS AND CHANGES IN NET ASSETS

For the year ended June 30, 1996

(Dollars in Thousands)

Unrestricted revenues, gains/(losses) and other support:	
Net patient service revenue	\$ 74,097
Investment loss	(368)
Other revenue	<u>2,375</u>
Total revenues, gains/(losses) and other support	<u>76,104</u>
Expenses:	
Salaries, wages and fringe benefits	84,861
Materials, supplies and services	27,394
Depreciation and amortization	4,615
Interest	<u>109</u>
Total expenses	<u>116,979</u>
Net loss	(40,875)
Transfers from affiliates	<u>66,786</u>
Increase in unrestricted net assets	25,911
Net assets, beginning of year	<u>11,163</u>
Net assets, end of year	<u>\$ 37,074</u>

The accompanying notes are an integral part of the financial statements.

## ALLEGHENY INTEGRATED HEALTH GROUP

STATEMENT OF CASH FLOWS  
For the year ended June 30, 1996  
(Dollars in Thousands)

Cash flows from operating activities:	
Change in net assets	\$ 25,911
Adjustments to reconcile change in net assets	
to net cash used by operating activities:	
Depreciation and amortization	4,615
Net transfers from affiliates	(66,786)
Loss on investment in joint ventures	451
Increase/(decrease) in cash and cash equivalents from changes in:	
Short-term investments	3,988
Receivables	(10,408)
Prepaid expenses	(244)
Accounts payable and accrued expenses	1,536
Other	4,686
Net cash used by operating activities	<u>(36,251)</u>
Cash flows from investing activities:	
Acquisition of physician practice assets, net	(4,829)
Acquisition of property and equipment, net	(4,738)
Acquisition of physician practice intangible assets	<u>(16,385)</u>
Net cash used by investing activities	<u>(25,952)</u>
Cash flows from financing activities:	
Repayments of long-term debt	(1,031)
Transfers from affiliates	<u>66,786</u>
Net cash provided by financing activities	<u>65,755</u>
Net increase in cash and cash equivalents	3,552
Cash and cash equivalents, beginning of year	<u>(3,459)</u>
Cash and cash equivalents, end of year	<u>\$ 93</u>
Supplemental disclosure:	
Cash paid for interest	<u>\$ 161</u>

The accompanying notes are an integral part of the financial statements.

ALLEGHENY INTEGRATED HEALTH GROUP

NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

1. Organization:

Allegheny Integrated Health Group (AIHG) was incorporated in September, 1994 as a Pennsylvania nonprofit charitable organization. Allegheny Health, Education and Research Foundation (AHERF), a nonprofit organization, is the parent company of AIHG. AIHG is primarily responsible for the development and operation of a physician practice network.

AHERF is also the parent company of Allegheny General Hospital, Allegheny University of the Health Sciences (Allegheny University), Allegheny University Hospitals, St. Christopher's Hospital for Children (St. Christopher's), Diversified Health Group, Inc. and Allegheny Health Services Providers Insurance Company (AHSPIC).

AIHG's continued existence is dependent upon ongoing support from AHERF, which has represented that it will continue to support the operations of AIHG for the ensuing fiscal year.

2. Accounting Policies:

The significant accounting policies applied in preparing the accompanying financial statements are summarized below:

Accounting Changes:

In fiscal year 1996, AIHG adopted Financial Accounting Standards Board Statement (FAS), No. 117, "Financial Statements of Not-for-Profit Organizations." FAS 117 establishes uniform standards for general-purpose external financial statements of not-for-profit organizations and further requires the classification of net assets into three categories, unrestricted, temporarily restricted and permanently restricted. Currently all AIHG net assets are unrestricted.

Use of Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent



## ALLEGHENY INTEGRATED HEALTH GROUP

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)

assets and liabilities at the date of the financial statements. Estimates also affect the amounts reported as revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash Equivalents:

Cash and cash equivalents include highly liquid investments purchased with a maturity date of three months or less and deposits maintained with AHERF which are available to AIHG.

Investments and Investment Income:

Short-term investments are managed pursuant to a master trust arrangement (Master Trust) that includes the investments of other AHERF entities. Investments in the Master Trust consist primarily of government and corporate obligations and repurchase agreements collateralized by U.S. Treasury notes and bonds that have fixed rates of return. Investment income and gains or losses are allocated on the pro rata cost value of each entity's investment. AIHG's pro rata share of the Master Trust is stated at fair value.

Property and Equipment:

Property and equipment, along with expenditures that extend the useful lives of assets, are recorded at cost. Maintenance and repairs are charged to expense as incurred. At the time assets are retired or otherwise disposed of, the cost thereof and the related accumulated depreciation or amortization are eliminated and any resulting gain or loss on disposition is recorded as other revenue.

Depreciation is provided over the estimated useful lives of the assets computed under the straight-line method with one-half year of depreciation recognized in the year the related assets are placed into service.

## ALLEGHENY INTEGRATED HEALTH GROUP

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)Other Assets:

Other assets consist primarily of intangibles associated with the purchase of physician practices. The intangibles are being amortized on a straight-line basis over periods ranging from 5-15 years. AIHG has a 50% ownership interest in East Net, Inc., which owns and operates physician practices. AIHG's share of loss from its East Net, Inc. investment for fiscal year 1996 was \$605.

Net Patient Service Revenue:

AIHG has agreements with third-party payors that provide for payments to AIHG at amounts different from its established rates. Payment arrangements include prospectively determined rates per procedure, discounted charges and capitation arrangements. Net patient service revenue is reported at the estimated net realizable amounts due from patients, third party payors, and others for services rendered. Any subsequent adjustments are recorded in future periods as final amounts are determined.

Related Party Transactions:

Fees charged for services provided by affiliates are included in expenses with all other transactions among affiliates recorded as net asset transfers on the statement of operations and changes in net assets. Any resulting amounts due to or from affiliates are settled periodically in the normal course of business.

Income Tax:

AIHG is a not-for-profit corporation that has applied for tax exempt status pursuant to Section 501 (C)(3) of the Internal Revenue Code.

## ALLEGHENY INTEGRATED HEALTH GROUP

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

3. Property and Equipment:

Property and equipment consists of the following components at June 30, 1996:

Buildings and lease-hold improvements	\$ 1,802
Equipment	<u>15,840</u>
	17,642
Less accumulated depreciation and amortization	<u>3,402</u>
	14,240
Construction in progress	<u>1,402</u>
Property and equipment, net	<u>\$ 15,642</u>

4. Current Portion of Long-Term Debt:

The current portion of long-term debt consists of the following obligations at June 30, 1996:

Promissory Notes:	
Maturity date of March 20, 1997 with interest at 6.0%	\$ 224
Maturity date of October 11, 1996 with interest at 8.0%	<u>872</u>
Current portion of long-term debt	<u>\$ 1,096</u>

5. Commitments:

In October 1991, AHERF entered into an agreement to manage the Sidney Hillman Medical Center (SHMC) for a 20 year period. SHMC provides primary and speciality care physician services primarily to members of the garment workers union. Under the terms of the agreement, AIHG subsidizes certain operating losses of SHMC. During fiscal year 1996, such subsidies amounted to \$791.

## ALLEGHENY INTEGRATED HEALTH GROUP

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

5. Commitments: (continued)

AIHG leases certain medical and office equipment and office space used in its operations. Rental expenses for operating leases for the fiscal year ended June 30, 1996 were \$6,014. The annual and total future minimum lease payments under noncancelable operating leases entered into as of June 30, 1996 are as follows:

<u>Year</u>	
1997	\$ 7,451
1998	7,629
1999	7,910
2000	6,972
2001	2,780
2002 and thereafter	<u>1,471</u>
Total minimum payments	<u>\$ 34,213</u>

6. Net Patient Service Revenue:

Net patient service revenue consists of the following components for the year ended June 30, 1996:

Gross patient service revenue	\$ 123,897
Less provisions for contractual adjustments	<u>49,800</u>
Net patient service revenue	<u>\$ 74,097</u>

Contractual adjustments represent the difference between standard billing rates and amounts estimated to be paid under various health benefit agreements. Provisions for contractual adjustments are recorded in the period in which the services are provided.

During fiscal year 1996, AIHG's bad debt expense amounted to \$1,137, which is included in materials, supplies and services expense on the statement of operations and changes in net assets.

## ALLEGHENY INTEGRATED HEALTH GROUP

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

**7. Insurance:**

AHERF is self-insured for primary coverage and for certain levels of excess coverage related to professional and general liability claims through AHSPIC, an affiliated captive insurance company incorporated in the Cayman Islands. In addition, AHERF participates in the Medical Professional Liability Catastrophic Loss Fund of the Commonwealth of Pennsylvania (CAT Fund) and maintains insurance under commercially insured programs on a claims-made basis for amounts in excess of the self-insurance and CAT Fund coverages. Premiums paid by AHERF to AHSPIC are retrospectively rated and are based on funding requirements determined by independent insurance actuaries to include provisions for estimates of the ultimate costs for both reported claims and claims incurred but not reported, determined on a discounted basis using a 7.5% rate. Professional and general liability expense is allocated by AHERF to each relevant AHERF entity based principally upon such entity's reported claims and estimated claims incurred but not reported. During fiscal year 1996, AIHG's total professional and general liability insurance expense was \$874.

AHERF is also self-insured for workers' compensation liability claims and has established a trust fund for the payment of such claims. Funding requirements and estimates of losses incurred are determined on a discounted basis using actuarial assumptions which include a 6.0% discount rate and which are subject to revisions based upon actual experience. Workers' compensation expense is allocated by AHERF to each relevant AHERF entity based principally upon such entity's reported claims and estimated claims incurred but not reported. During fiscal year 1996, AIHG's workers' compensation expense was \$125.

**8. Pension Plans:**

AHERF maintains a noncontributory, defined benefit pension plan covering substantially all AIHG employees. Under this cash balance plan (the Plan), pension accruals are determined using a defined percentage of an employee's current compensation based on the employee's age and years of service. Each employee's individual retirement benefit is defined within the Plan's obligation as a notational cash balance retirement account and is credited with interest based on a defined interest rate. AHERF's funding policy is to

ALLEGHENY INTEGRATED HEALTH GROUP

NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

8. Pension Plans: (continued)

contribute such amounts as are necessary on an actuarial basis to provide the Plan with assets sufficient to meet benefits to be paid to retirees or their beneficiaries and to satisfy the minimum funding requirements of the Employee Retirement Income Security Act of 1974. Pension expense is allocated by AHERF to each relevant AHERF entity based principally upon the number of full and part time employees covered by the Plan and their respective salary levels. During fiscal year 1996, AIHG's pension expense was \$46.

AHERF sponsors a contributory, defined contribution savings plan which is available to substantially all AIHG employees in order to provide additional security during retirement by creating an incentive for employees to make regular contributions on their own behalf. Under this plan, and as determined on an individual employee basis, AHERF contributes amounts equal to 25% of an employee's contribution for employee contributions up to 4% of such employee's salary in a given year. Such expense is allocated by AHERF to each relevant AHERF entity based on actual contributions made. AIHG's expense associated with contributions to this savings plan was \$71 for the year ended June 30, 1996.

9. Related Party Transactions:

During fiscal year 1996, AIHG purchased staff and physician services, supplies and other miscellaneous services from various AHERF entities, as follows:

Entity	Salaries, Wages and Fringe Benefits	Materials, Supplies and Services	Total
AGH	\$ 746	\$ 29	\$ 775
Delaware Valley Obligated Group	58,119	2,293	60,412
AHERF	4,599	889	5,488

During fiscal year 1996, AHERF transferred \$66,786 to AIHG to support its acquisition and operation of physician practices. These transfers have been reflected as net asset transfers on the statement of operations and changes in net assets.

## ALLEGHENY INTEGRATED HEALTH GROUP

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

10. Functional Expenses:

AIHG provides general health care services through its physician practice network. Expenses related to these services are as follows for the year ended June 30, 1996:

Health care services	\$ 100,949
General and administrative	<u>16,030</u>
	<u>\$ 116,979</u>

11. Concentrations of Credit Risk:

AIHG grants credit without collateral to its patients, most of whom are local residents insured under third-party payor agreements. The mix of receivables from patients and third-party payors is as follows at June 30, 1996:

Medicare	19%
Medicaid	5
Blue Shield	22
Managed Care	3
Other third-party payors	34
Patients	<u>17</u>
	<u>100%</u>

12. Fair Value of Financial Instruments:

The following methods and assumptions were used by AIHG in estimating the fair value of its financial instruments:

**Cash and cash equivalents:** The carrying value reported in the balance sheet for cash and cash equivalents approximates its fair value.

**Short-term investments:** The carrying value reported in the balance sheet for short-term investments approximates its fair value.

**Long-term debt:** The carrying value reported in the balance sheet for long-term debt approximates its fair value.

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**Allegheny-Singer Research Institute**

*Financial*

*Statements*

*for the*

*year ended*

*June 30, 1996*

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**GOV 56038**



## ALLEGHENY-SINGER RESEARCH INSTITUTE

BALANCE SHEET  
June 30, 1996  
(Dollars in Thousands)

## ASSETS

Current assets:	
Cash and cash equivalents	\$ 710
Short-term investments	4,939
Grants and other receivables	2,727
Prepaid assets	<u>6</u>
Total current assets	8,382
Investments	12,268
Property and equipment, net	13,495
Due from affiliates	1,241
Other assets	<u>1,354</u>
Total assets	<u>\$ 36,740</u>

## LIABILITIES AND NET ASSETS

Current liabilities:	
Accounts payable and accrued expenses	\$ 3,276
Deferred grant revenue	<u>3,717</u>
Total current liabilities	6,993
Deferred grant revenue	<u>1,074</u>
Total liabilities	8,067
Net assets:	
Unrestricted	18,229
Restricted:	
Temporarily	4,458
Permanently	<u>5,986</u>
Total net assets	<u>28,673</u>
Total liabilities and net assets	<u>\$ 36,740</u>

The accompanying notes are an integral part of the financial statements.

## ALLEGHENY-SINGER RESEARCH INSTITUTE

## STATEMENT OF CHANGES IN NET ASSETS

For the year ended June 30, 1996

(Dollars in Thousands)

## Unrestricted net assets:

Net loss	\$ (14,180)
Transfers from deferred revenue	562
Deferred revenue used for acquisition of property and equipment	999
Net assets released from restrictions used for acquisition of property and equipment	11
Transfers from affiliates, net	<u>19,471</u>
Increase in unrestricted net assets	<u>6,863</u>

## Temporarily restricted net assets:

Adjustment from change in accounting principles	954
Contributions	1,061
Investment income	1,300
Unrealized appreciation of investments	653
Net assets released from restrictions	<u>(1,691)</u>
Increase in temporarily restricted net assets	<u>2,277</u>

## Permanently restricted net assets:

Contributions	<u>146</u>
Increase in permanently restricted net assets	<u>146</u>

## Increase in net assets

Net assets, beginning of year	9,286
	<u>19,387</u>
Net assets, end of year	<u>\$ 28,673</u>

The accompanying notes are an integral part of the financial statements.

## ALLEGHENY-SINGER RESEARCH INSTITUTE

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)

Unrestricted - Net assets that are not subject to donor-imposed stipulations. Such net assets may be designated by the Board of Trustees for specific purposes or limited by contractual agreements with outside parties.

Temporarily Restricted - Net assets whose use is subject to donor-imposed stipulations that can be fulfilled by specific actions pursuant to such stipulations or expire by the passage of time.

Permanently Restricted - Net assets subject to donor-imposed stipulations that neither expire by passage of time nor can be fulfilled and removed by action. Such net assets, which must be maintained in perpetuity, generally include only the original amount of the contribution since the donors of these assets most often permit the use of all investment earnings for specific or general purposes.

FAS 124 requires that investments in equity securities with readily determinable fair values and all investments in debt securities be reported at fair value with gains and losses included in the statement of operations. As permitted by FAS 124, the cumulative effect of adopting this statement for periods prior to July 1, 1995 for investments temporarily restricted is \$954 and is reflected on the statement of changes in net assets.

Use of Estimates:

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. Estimates also affect the amounts reported as revenues and expenses during the reporting period. Actual results could differ from those estimates.

## ALLEGHENY-SINGER RESEARCH INSTITUTE

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

2. Accounting Policies: (continued)Property and Equipment:

Property and equipment, along with expenditures that extend the useful lives of assets, are recorded at cost. Maintenance and repairs are charged to expense as incurred. At the time assets are retired or otherwise disposed of, the cost thereof and the related accumulated depreciation or amortization are eliminated and any resulting gain or loss on disposition is recorded as other revenue.

Depreciation is provided over the estimated useful life of the assets computed under the straight-line method with one-half year of depreciation recognized in the year the related assets are placed into service.

Other Assets:

Other assets consist primarily of patents that are being amortized over five years using the straight-line method and an investment in a licensing agreement to develop cardiac assist devices.

Restricted Net Assets:

Temporarily restricted net assets are those whose use has been limited by donors for a specific purpose or a specific time period. Permanently restricted net assets have been restricted by donors to be maintained in perpetuity. Temporarily restricted assets released from restriction during the period are reflected in the statement of operations.

Related Party Transactions:

Fees charged for services provided by affiliates are included in expenses with all other transactions among affiliates recorded as net asset transfers. Any resulting accounts receivable or payable with affiliates are settled periodically in the normal course of business.

Income Tax:

ASRI has been recognized as tax exempt pursuant to Section 501 (c)(3) of the Internal Revenue Code.

## ALLEGHENY-SINGER RESEARCH INSTITUTE

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

3. Investments:

The following table sets forth the composition of investments by investment type at June 30, 1996:

## Unrestricted:

Cash and short-term investments	\$ 94
Government and corporate obligations	407
Marketable equity securities	<u>1,311</u>
	1,812

## Temporarily Restricted:

Cash and short-term investments	76
Government and corporate obligations	1,064
Marketable equity securities	<u>3,330</u>
	4,470

## Permanently Restricted:

Cash and short-term investments	121
Government and corporate obligations	2,408
Marketable equity securities	<u>3,457</u>
	<u>5,986</u>
Investments	<u>\$ 12,268</u>

Investment returns consisted of the following for the year ended June 30, 1996:

Net gains on investments	\$ 41
Dividends and interest	<u>17</u>
	<u>\$ 58</u>

4. Property and Equipment:

Property and equipment consists of the following components at June 30, 1996:

Building improvements	\$ 9,070
Equipment	<u>14,680</u>
	23,750
Less accumulated depreciation and amortization	<u>10,255</u>
Property and equipment, net	<u>\$ 13,495</u>

## ALLEGHENY-SINGER RESEARCH INSTITUTE

## NOTES TO FINANCIAL STATEMENTS

June 30, 1996

(Dollars in Thousands)

**7. Pension Plan:**

AHERF maintains a noncontributory, defined benefit pension plan covering substantially all ASRI employees. Under this cash balance plan (the Plan), pension accruals are determined using a defined percentage of an employee's current compensation based on the employee's age and years of service. Each employee's individual retirement benefit is defined within the Plan's obligation as a notational cash balance retirement account and is credited with interest based on a defined interest rate. AHERF's funding policy is to contribute such amounts as are necessary on an actuarial basis to provide the Plan with assets sufficient to meet benefits to be paid to retirees or their beneficiaries and to satisfy the minimum funding requirements of the Employee Retirement Income Security Act of 1974. Pension expense is allocated by AHERF to each relevant AHERF entity based principally upon the number of full and part time employees covered by the Plan and their respective salary levels. During fiscal year 1996, ASRI's pension expense was \$2.

AHERF sponsors a contributory, defined contribution savings plan which is available to substantially all ASRI employees in order to provide additional security during retirement by creating an incentive for employees to make regular contributions on their own behalf. Under this plan, and as determined on an individual employee basis, AHERF contributes an amount equal to 25% of an employee's contribution for an employee contribution up to 4% of such employee's salary in a given year. Such expense is allocated by AHERF to each relevant AHERF entity based on actual contributions made. ASRI's expense associated with contributions to this savings plan was \$97 for the year ended June 30, 1996.

**8. Related Party Transactions:**

ASRI exercises control over Allegheny Heart Institute (AHI), a Pennsylvania non-profit organization whose principal purpose is to fund specific research initiatives at ASRI. During fiscal year 1996, AHI provided funding to ASRI of \$10. AHI had net income of \$131, cash and cash equivalents of \$23, short-term investments of \$659 and net assets of \$682 as of June 30, 1996. The financial position and statement of operations of AHI have not been combined with ASRI as of June 30, 1996.

**ALLEGHENY-SINGER RESEARCH INSTITUTE****NOTES TO FINANCIAL STATEMENTS**

June 30, 1996

(Dollars in Thousands)

**9. Functional Expenses:**

ASRI performs medical research through its research institute. Expenses related to these services are as follows for the year ended June 30, 1996:

Medical research	\$ 21,891
General and administrative	<u>4,902</u>
	<u>\$ 26,793</u>

**10. Fair Value of Financial Instruments:**

The following methods and assumptions were used by ASRI in estimating the fair value of its financial instruments:

**Short-term Investments:** The carrying value reported in the balance sheet for short-term investments approximates its fair value.

**Investments:** These assets consist primarily of government and corporate obligations and marketable equity securities. Fair values were determined based on quoted market prices and dealer quotes where available, or quoted market prices pertaining to similar securities where not available. The carrying value reported on the balance sheet for investments approximate their fair value.

**11. Indirect Costs:**

ASRI's approved two-year, predetermined indirect cost rate of 52% plus fringe benefits at 19.4%, was effective from July 1, 1992 through June 30, 1994; subsequent to this period, these rates are provisional until renegotiated and approved. The predetermined fixed rate was determined based on ASRI's financial information as of June 30, 1991 and for the year then ended. ASRI has continued to utilize the established provisional rate through June 30, 1996.

Coopers  
& Lybrand

Coopers &amp; Lybrand L.L.P.

a professional services firm

Report of Independent Accountants

To the Board of Trustees of  
Allegheny General Hospital:

We have audited, in accordance with generally accepted auditing standards, the consolidated balance sheet of Allegheny General Hospital, hereinafter referred to as the Obligated Group, as of June 30, 1996, and the related consolidated statement of operations, changes in net assets, and cash flows for the year then ended, and have issued our report thereon dated September 11, 1996. The Obligated Group includes the accounts of Allegheny General Hospital and Allegheny-Singer Research Institute.

In connection with our audit, nothing came to our attention that caused us to believe that the Obligated Group was not in compliance with the covenants (insofar as they relate to accounting matters) contained in Article V of the Restated and Amended Master Trust Indenture dated April 7, 1993 (as supplemented and amended) with PNC Bank (as Master Trustee). It should be noted, however, that our audit was not directed primarily toward obtaining knowledge of such noncompliance.

This report is intended solely for the information and use of the Board of Trustees and management of the Obligated Group and PNC Bank and should not be used for any other purpose.

*Coopers & Lybrand L.L.P.*

Pittsburgh, Pennsylvania  
September 11, 1996



Coopers  
& Lybrand

a professional services firm

Report of Independent Accountants

To the Board of Trustees of  
Allegheny University Hospitals,  
Allegheny University of the Health Sciences  
and St. Christopher's Hospital for Children:

We have audited, in accordance with generally accepted auditing standards, the combined balance sheet of the Delaware Valley Obligated Group, hereinafter referred to as the Obligated Group, as of June 30, 1996, and the related combined statement of operations, changes in net assets, and cash flows for the year then ended, and have issued our report thereon dated September 11, 1996.

In connection with our audit, nothing came to our attention that caused us to believe that the Obligated Group was not in compliance with the covenants (insofar as they relate to accounting matters) contained in Article 6 of the Master Trust Indenture and Sections 3.6 and 3.21 of the First Supplemental Master Trust Indenture dated May 15, 1996 with Norwest Bank, Minnesota, N.A. (as Master Trustee). It should be noted, however, that our audit was not directed primarily toward obtaining knowledge of such noncompliance.

This report is intended solely for the information and use of the Board of Trustees and management of the Obligated Group and Norwest Bank, Minnesota, N.A. and should not be used for any other purpose.

*Coopers & Lybrand L.L.P.*

Pittsburgh, Pennsylvania  
September 11, 1996

**EXHIBIT 0807**